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C O N F I D E N T I A L SECTION 01 OF 02 YEREVAN 001238

SIPDIS

EUR/CACEN FOR EUGENIA SIDERAS, EUR/ACE FOR MARIA LONGI,  
DEPARTMENT PLEASE PASS USAID, DEPARTMENT PLEASE PASS  
MILLENNIUM CHALLENGE CORPORATION

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SUBJECT: KOCHARIAN DISCUSSES REFORMS, ARMENIA'S ECONOMIC  
FUTURE AND MCA WITH EUR/ACE AMBASSADOR PASCUAL

Classified By: Ambassador John Ordway for reasons 1.5 (b) and (d).

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SUMMARY  
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1. (SBU) EUR/ACE Ambassador Carlos Pascual, accompanied by the Ambassador, met with President Robert Kocharian May 18 following the meetings of the U.S.-Armenia Task Force on Economic Cooperation (USATF). The meeting focused on the potential role for Armenia as an example of progress and freedom in the region, ways to improve economic conditions, protecting civil liberties and fighting corruption. The discussion also included Armenia's recently announced eligibility for funding through the Millennium Challenge Account (MCA). Kocharian defended the GOAM's record on rule of law and touted recent economic growth as indicative of Armenia's ongoing progress. End Summary.

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KOCHARIAN DEFENDS GOAM PROGRESS ON COE COMMITMENTS  
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2. (SBU) EUR/ACE Ambassador Carlos Pascual, accompanied by Ambassador Ordway, met with President Robert Kocharian May 18 following the final session of the U.S.-Armenia Task Force on Economic Cooperation (USATF). Also present at the meeting were Minister of Finance and Economy Vardan Khachatryan, Deputy Minister of Foreign Affairs Ruben Shugarian and Chief Economic Advisor Vahram Nercissiantz.

3. (C) Ambassador Pascual opened the meeting with a discussion of the link between democratic and economic reforms and the general "neighborhood" in which the world classifies and views Armenia. Discussion centered around the need for the GOAM to perform along the lines of northern tier European countries if it wanted to be considered part of their league. Kocharian reacted to Ambassador Pascual's call on the GOAM to accelerate reforms and stand out as a leader among neighboring countries by enumerating a lengthy list of GOAM initiatives keyed to Armenia's Council of Europe obligations. He pointed to the privatization of major industries, recent anti-monopoly legislation, private property disclosure laws, civil service reform and efforts to de-centralize the power structure of government bureaucracies as proof that GOAM was "well on its way toward Europe." Kocharian argued that democracy in Armenia was inextricably tied to economic opportunity and the possibility of more jobs and a better standard of living. Ambassador Pascual responded that increased economic opportunities would come to Armenia if the GOAM made the internal changes necessary for an image as a fully democratic state.

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SIDES DISCUSS BANKING SECTOR, CORRUPTION  
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4. (C) The meeting included a discussion of issues related to reforms in the banking sector, highlighting it as one of the most important economic issues Armenia currently faces. Both sides discussed the conclusions of the May 17-18 meetings of the U.S.-Armenia Task Force on Economic Cooperation (USATF) including the need to increase lending as a percentage of GDP and address impediments to lending. Ambassador Pascual highlighted the fact that a lack of financial intermediation locally would preclude sustainable growth and diversification in the Armenian economy. He underlined the need for legislation on collateral rights and said that the USG and GOAM would cooperate on these issues following the completion of the USAID-sponsored financial sector study being coordinated with the World Bank and International Monetary Fund.

5. (C) In response to Kocharian's outline of the GOAM's recently adopted anti-corruption strategy, Ambassadors Ordway and Pascual suggested that the GOAM first take concrete actions that would resonate among the Armenian population as a whole and lend credibility to the strategy and signal real commitment from the government. The sides discussed possibilities for such initiatives in areas that impact the

lives of everyday citizens, including law enforcement. Ambassador Pascual pressed for action in Armenia's courts and said that corrupt individuals needed to fear a risk of imprisonment for corrupt behavior. Kocharian expressed concern regarding this last point, responding that he would rather find ways to "eliminate the roadblocks that cause corruption." His comments suggested that he would prefer to address the issue systematically rather than crack down on corrupt individuals in positions of authority or economic influence.

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KOCHARIAN ON MCA: "WE'RE READY TO GO"  
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16. (C) Kocharian reacted enthusiastically to news of the visit to Armenia of MCC CEO Applegarth and his delegation scheduled for early June. He said that the GOAM was "ready to go" and was already making preparations for an MCA compact submission, including the designation of a local board of directors (likely headed by the Prime Minister) and sponsoring preliminary discussions among appropriate ministries regarding areas of greatest need. Kocharian said he was committed to the need for broad consultation with civil society during the process of developing an MCA compact submission. When informed that regression in important areas involving democracy and governance could potentially reverse a country's MCA eligibility, Kocharian stated emphatically that the GOAM had actually made progress in terms of individual freedoms. While generally skeptical of the organizations or methods used to obtain MCA indicators, Kocharian said he was confident that Armenia's scores would only improve in these areas.

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IMPLEMENTING USATF CONCLUSIONS VAT REFUNDS  
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17. (C) During a discussion of conclusions from the recent USATF meetings, Kocharian recognized that some U.S. business had complained about the need for quicker, more complete VAT refunds. He said, however, that the GOAM was concerned that tax fraud, including bogus transfers of VAT refund eligibility among businesses, could represent a major drain on potential state income. He thanked the USG for its offer to work with the GOAM to address these issues.

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COMMENT  
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18. (C) Kocharian's remarks indicate that he is acutely aware of international criticism after the fallout of the mid-April opposition rallies in Armenia. While citing MCA eligibility as a positive evaluation of the country, he simultaneously expressed somewhat defeatist views of his domestic and international reputation at the moment. His opinion that, "Either way I appear to be guilty," however, does not seem to have hampered his pro-active approach to the process of developing an MCA compact. He appears to be investing political capital and listening carefully to signs from Washington regarding MCA so that a full team is in place to greet the MCC delegation in early June.

19. (U) Ambassador Pascual has cleared on this message.  
ORDWAY